

STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petition	:	
of	:	
CONCENTRIC NETWORK CORPORATION	:	DETERMINATION
	:	DTA #819533
for Revision of a Determination or for Refund of Sales	:	
and Use Taxes under Articles 28 and 29 of the Tax Law	:	
for the Years 1999 and 2000.	:	

Petitioner, Concentric Network Corporation, c/o Michael O'Day, XO Communications, 11111 Sunset Hills Road, Reston, Virginia 20190, filed a petition for revision of a determination or for refund of sales and use taxes under Articles 28 and 29 of the Tax Law for the years 1999 and 2000.

A hearing was held before Brian L. Friedman, Administrative Law Judge, at the offices of the Division of Tax Appeals, 641 Lexington Avenue, New York, New York, on March 2, 2004 at 10:30 A.M., with all briefs to be submitted by July 26, 2004, which date began the six-month period for the issuance of this determination. Petitioner appeared by Anderson, Gulotta & Hicks, P.C. (Michael A. Warnagiris, Esq., of counsel). The Division of Taxation appeared by Christopher C. O'Brien, Esq. (James Della Porta and Lori P. Antolick, Esqs., of counsel).

ISSUES

I. Whether the Division of Taxation properly denied petitioner's claim for refund of sales and use taxes on its purchases of line access charges from MCI Worldcom, Frontier and Eagle Communications on the basis that such services were intrastate telephone services subject to tax pursuant to Tax Law § 1105(b)(1)(B).

II. Whether, if determined to be subject to tax as purchases of telephony or telegraphy, such services are nevertheless exempt from tax on the basis that they were used by petitioner to provide its customers with internet access which, by its very nature, is an interstate activity exempt from taxation.

FINDINGS OF FACT

In its brief filed on May 11, 2004, petitioner submitted 15 proposed findings of fact, each of which has been substantially incorporated into the following Findings of Fact:

1. On February 25, 2002, the Division of Taxation (“Division”) received from Concentric Network Corporation (“Concentric”) an Application for Credit or Refund of Sales and Use Tax which claimed a refund in the amount of \$438,960.26. The application stated that Concentric, a company wholly owned by XO Communications (Concentric was purchased by XO Communications, formerly Nextlink, Inc., in 2000), is located at various locations throughout the State of New York and is engaged in the business of providing internet service to customers located in New York. The refund claim involved sales tax paid by Concentric on tangible personal property, including equipment and dial-up access, in connection with its delivery of internet services.

The bases upon which Concentric claimed exemption from tax were: (a) that pursuant to Tax Law § 1115(a)(12) for the period prior to 2000 and pursuant to Tax Law § 1115(a)(12-a) thereafter (actually after September 1, 2000, the effective date of the enactment of paragraph 12-a), its purchase of equipment used directly to provide internet access service was exempt; and (b)

that pursuant to Tax Law § 1105(b)(1), sales for resale of telephone service are not subject to tax.¹

2. On September 30, 2002, the Division denied, in full, Concentric's claim for refund of sales tax stating as follows:

There are three issues involved in this refund denial:

1. Part of the refund is for periods beyond the time this company filed sales tax returns and paid sales tax. (The company's ownership and ID number changed in August 2000.)
2. ISP² equipment was not exempt from sales and use tax prior to September 2000.
3. Telephone charges are not exempt when an ISP pays them, even though they bill their customers an internet access charge.

3. Due to the fact that Concentric merged into XO Communications in August 2000, the claim for refund was revised from its original amount of \$438,960.26 to \$272,113.42 to reflect only those amounts of tax paid prior to the merger, i.e., all of the transactions at issue occurred during the years 1999 and 2000. Transactions occurring after 2000 were included in a separate claim for refund which is not at issue in this proceeding.

At the hearing, Concentric introduced into evidence a summary of all of the invoices upon which sales tax was paid by Concentric and for which the claim for refund was based. This summary listed: a reference number, the name of the vendor to whom tax was paid, the date of the invoice, a description of what was purchased (examples included: "private line," "dial access," "Colo Class III Pops," etc), invoice amount, amount paid, Federal tax, State sales tax,

¹ Concentric's assertion that its purchases were exempt because they were for resale was apparently withdrawn since at the hearing and in its brief and reply brief, it contended that its purchases were not subject to tax because such purchases were not properly classified by the Division as telephony or telegraphy.

² The abbreviation "ISP" refers to an Internet Service Provider.

local sales tax and refund requested (the amount of refund was the sum of State and local sales tax paid). The summary also contained a column entitled "Comments." Under this column were listed the locations of the line access purchased by Concentric which, in all cases, were New York locations. The locations listed included: "New York," "Buffalo, New York," "New York(Hudson)," "New York City, New York " and Syracuse, N.Y."

4. During the period from February 1999 until June 2000, Concentric purchased channelized T-1 lines and ATM lines from MCI Worldcom, Eagle Communications and Frontier. A T-1 or Trunk Level 1 is a digital transmission link with a total signaling speed of 1.544 Mbps (1,544,000 bits per second which may be divided into up to 24 separate voice-quality channels or which may be utilized as a single two-way high speed data stream). An ATM or Asynchronous Transfer Mode is a layered networking protocol which allows for a single physical line to be used to connect multiple destinations.

5. The internet is the worldwide interconnected system of packet-switched computer networks that connects computers and facilitates the exchange of data and information.

6. An ISP or Internet Service Provider is a vendor whose primary function is to provide its customers with access to the internet and world wide web along with other secondary functions such as providing electronic mail accounts.

7. The Internet Backbone is the high-speed network which spans the world from one metropolitan area to another.

8. National Access Points or NAPs are interconnection points where the lines that form the internet backbone are linked and where local ISPs must connect in order to carry their customer's data traffic to the internet backbone.

9. TCP/IP Protocol stands for Transmission Control Protocol/Internet Protocol. Internet Protocol defines how information is broken down into packets and routed. Transmission Control Protocol adds reliability to the IP packets which helps the packets reach their destination in the proper fashion.

10. T-3 or Trunk Level 3 is a digital transmission link with a total signaling speed of 44.736 Mbps with a capacity equivalent to 28 T-1 lines.

11. A packet switched network allows the same computer to send and receive data packets to and from multiple sources simultaneously. It is not necessary for a direct connection to be established in order for two computers to communicate with one another over the internet. This network differs from circuit switched networks or traditional phone networks which require a continuous connection.

12. A POP or Point of Presence is a facility where local internet traffic is aggregated. A Super POP is a combination point of all of the aggregated traffic for delivery to the internet backbone.

13. During 1999 and 2000, Concentric did not provide voice products or switch traditional voice traffic of any kind.

14. In all cases, internet traffic on Concentric's network, originating in New York and other states, was routed through Washington D.C. or Chicago, Illinois before reaching its destination.

15. Any ISP could insure that all of its traffic was routed both inside and outside a particular state by locating a router and related equipment in at least two states.

16. Michael Scott who is employed by Access Communications and was a director of access technology at Concentric until approximately 2002 appeared at the hearing and was

qualified as an expert witness in the area of internet access. He participated in the creation of the commercial entity known as the “internet.” In 1993, Mr. Scott and two other individuals started Concentric, initially offering internet e-mail and then offering more interactive internet services where people could chat with each other, exchange files and use other computer systems. In 1994, they built their own internet network because it became too expensive to pay Sprint for dial-up service. In 1995, network upgrades were made to prepare for the worldwide web. After April 30, 1995, the internet was privatized; previously, the National Science Foundation operated the internet backbone and controlled access to the internet. In 1996, with the passage of the Telecommunications Act, competitive local exchange carriers were created and Mr. Scott and his associates began a company called MFS Communications which was eventually acquired by World Com. MFS Communications was a pioneer in the network architecture specifically for ISPs. In 1997, MFS Communications worked with SBC Communications to launch digital subscriber line service (DSL) which is a high-speed form of internet access which was competitively priced to compete with dial-up internet service. In 1998, Concentric purchased Internex Information Services, a national entity which had pairing arrangements with 35 or 40 different ISPs across the United States which allowed Concentric to become a Tier 1 ISP which is not dependent upon traffic with other internet service providers. In June 2000, Concentric merged with Nexlink Communications and later that year changed its name to XO Communications.

17. Mr. Scott explained that when one dials into or connects to the internet, there is an engine for every computer that is connected to the internet and that can “talk to” other computers. That process is done through creating packets which are collections of data. The

internet is made up of thousands of devices called routers which are responsible for taking bits of information and passing them through the communication links that make up the entire internet.

There are a collection of ISPs that make up the internet backbone. The internet categorizes ISPs as Tier 1, 2 or 3. A Tier 1 ISP is the largest and is an ISP that maintains a relationship with all of the other ISPs in the internet, i.e., it talks to everyone. After its purchase of Internex, Concentric was considered to be a Tier 1 ISP and had the network facilities to operate the internet network across the United States.

A Network Access Point is the facility at which all of the ISPs come together to exchange traffic with each other and to interconnect their networks. There were three original network access points: Pentsauken, New Jersey, Chicago, Illinois and San Francisco, California.

18. Mr. Scott indicated that a traditional telephone network is made up of a circuit switch technology which means that the network sets up a phone call in such a fashion that there is a reserved amount of space or bandwidth to cross that telecommunication network for the call to occupy. With packet switch networks which are utilized when computers are communicating across the internet, there is no fixed amount of band allocated for that session. The bandwidth is used as it is needed thereby making it more efficient. There is a telephone aspect of dial-up internet access which is that portion that connects one to the telephone where calls are received and routers answer those calls.

19. While all of the invoices at issue were introduced into evidence at the hearing, Concentric also introduced into evidence, as a separate exhibit, a packet of selected invoices which were referenced by Mr. Scott during his testimony. For example, the invoice labeled "1710A" is an invoice from MFS Worldcom, dated November 1, 1999, which describes the item purchased by Concentric, for the sum of \$756.00, as "COLO Class III Pops" which Mr. Scott

indicated was the cost associated with Concentric's co-location (putting the equipment into someone else's facility) of equipment into the City of Buffalo with World Com. It must also be noted that this invoice, under the heading "BAN DESCRIPTION" states "PRIVATE LINE BUFFALO."

The invoice labeled "1768A" is an invoice from MFS Worldcom which bills Concentric for the sum of \$55,354.53 for six different items. Mr. Scott indicated that the invoice was related to the ATM network connectivity that Concentric's super POP has in Hillburn, New York. Mr. Scott described the first of the six items, "BB ATM Access - MCI," as representing two circuits, one which goes to Washington, D.C. and the other to Chicago, Illinois. The next two items, "INTERNET MCI" and "INTERNET Other" could not be identified by Mr. Scott. The final three items on the invoice, "DAF installation," "DAF local loop" and "DAF infrastructure," were described by Mr. Scott as the infrastructure for the ATM network, the "port level" costs for the virtual circuits and virtual paths.

Invoice "1773E," an invoice from MFS Telecom, Inc., dated April 1, 1999, is part of a larger invoice for new charges totaling \$23,602.04 (including taxes and finance charges) which is labeled "1773B." The first two charges on invoice 1773E were described by Mr. Scott as charges associated with the DSL base internet access product, customer circuits. Invoice "1773G and "1773H" list the customers of Concentric's internet services.

Invoice "2268C" contains charges (current charges are \$822.20) billed to Concentric by Frontier, dated August 28, 1999, for channelized T1 service in Rochester, New York. These charges include fees for "VP Flat Rate T1 Link" and "VP T1 Channel Termination." This invoice indicates that the charges are for monthly service for the period August 28, 1999 through

September 27, 1999. Mr. Scott indicated that these services represent channelized T1 or the telephone line portion of Concentric's internet network in Rochester, New York.

Invoice "2838A" is an invoice dated January 12, 2000 from MFS Dial Access NY (Hudson) for dial access in the amount of \$12,326.26. Mr. Scott indicated that the invoice was for a facility at 60 Hudson Street in New York City and represented the dial-up portion of the internet network.

SUMMARY OF THE PARTIES' POSITIONS

20. Concentric's position may be summarized as follows:

a. Concentric's purchases of channelized Trunk Level I (T-1) and Asynchronous Transfer Mode (ATM) lines are not subject to sales tax because such purchases are not properly classified as telephony or telegraphy. It maintains that while these line types can be used to switch voice traffic, it did not provide voice products or switch traditional voice traffic of any kind during the period at issue. While the telephony and telegraphy are defined as the "use or operation of any apparatus for transmission of sound, sound reproduction or coded or other signals" (20 NYCRR 527.2[d][2]), Concentric does not transmit signals. In the internet context, transmission and receipt of data traffic occurs at the central processing unit of an end user's computer;

b. Concentric states that the lines at issue are component parts of its interstate product known as interstate access. Through the evidence produced at the hearing, Concentric contends that it has established that in all cases, internet traffic on its network, originating in New York (and other states), was routed through Washington, D.C. or Chicago, Illinois before reaching its destination. Internet service, by its very nature, is an interstate activity which is not subject to tax by New York State; and

c. Since the Tax Law imposes the sales tax upon every sale except interstate and international telephony and telegraphy and telephone and telegraph service (Tax Law § 1105[b][1][B]), to be exempt from taxation, Concentric need not establish that it resold telephony, only that it purchased interstate telephony. In the matter at issue, 100 percent of Concentric's internet traffic travels outside New York.

21. In response, the Division maintains that Concentric purchased *intrastate* telephone service from MCI Worldcom, Frontier and Eagle Communications and used this intrastate telephone service which it purchased to allow its customers to dial into and connect to the internet. While petitioner did not use the telephone lines to transmit voice communications, as noted in 20 NYCRR 527.2(d)(2), telephony includes "use or operation of any apparatus for transmission of sound, sound reproduction or coded or other signals." The Division states that the regulations clearly contemplate a situation where a taxpayer would purchase telephone lines from a communications carrier and then use the lines to provide a packet switched network to provided internet access to its customers.

The Division further contends that the interstate nature of the internet is irrelevant. Concentric was not selling telephone service (interstate or otherwise) or any other taxable service and its purchases were, therefore, not for resale. Accordingly, Concentric's use of the telephone service is irrelevant and has no bearing on the taxable status of the charges incurred by Concentric therefor.

CONCLUSIONS OF LAW

A. Tax Law § 1105(b)(1)(B) imposes sales tax upon the receipts from every sale, other than sales for resale, of "telephony and telegraphy and telephone and telegraph service of

whatever nature except interstate and international telephony and telegraphy and telephone and telegraph service”

20 NYCRR 527.2(a)(2) provides, in relevant, part that the words “of whatever nature” contained in Tax Law § 1105(b) “indicate that a broad construction is to be given the terms describing the items taxed.”

B. 20 NYCRR 527.2(d)(1) states that “[t]he provisions of section 1105(b) of the Tax Law with respect to telephony and telegraphy and telephone and telegraph service impose a tax on receipts from intrastate communication by means of devices *employing the principles of telephony and telegraphy*.” (Emphasis added.)

20 NYCRR 527.2(d)(2) provides as follows:

The term *telephony and telegraphy* includes use or operation of any apparatus for transmission of sound, sound reproduction or coded or other signals.”

* * *

Example 3: Message switching services, transmitted to a computer over lines leased from a communication carrier are telegraph services subject to the tax imposed under section 1105(b) of the Tax Law.

20 NYCRR 527.2(4) states:

A service is not considered telegraphy or telephony if either of these services is merely an incidental element of a different or other service purchased by the customer.

Example 6: A company offers its customers a protective service using a central station alarm system, which transmits signals telegraphically. The customer is purchasing a protective service.

C. Chapter 615 of the Laws of 1998 added a new section 179 of the Tax Law which provides as follows:

1. For purposes of this article, Internet access service shall not constitute a telecommunications service, nor shall the provision of Internet access service constitute the carrying on of a telephone, local telephone, telegraph, or transmission business.

2. The term 'Internet access service' shall have the meaning ascribed thereto in subdivision (v) of section eleven hundred fifteen of this chapter.

Chapter 615 of the Laws of 1998 also added a new subdivision (v) to section 1115 of the Tax Law (referred to in subdivision [2] of the new section 179 of the Tax Law hereinabove) which provides as follows:

(v) Receipts from the sale of Internet access service, including start-up charges, and the use of such service, shall be exempt from the taxes imposed under this article. For purposes of this subdivision, the term 'Internet access service' shall mean the service of providing connection to the Internet, but only where such service entails the routing of Internet traffic by means of accepted Internet protocols. The provision of communication or navigation software, an e-mail address, e-mail software, news headlines, space for a website and website services, or other such services, in conjunction with the provision of such connection to the Internet, where such services are merely incidental to the provision of such connection, shall be considered to be part of the provision of Internet access service.

D. Prior to September 1, 2000, Tax Law § 1115(a)(12), in relevant part, exempted from sales and use taxes:

telephone central office equipment or station apparatus or comparable telegraph equipment for use directly and predominantly in receiving at destination or initiating and switching telephone or telegraph communication or in receiving, amplifying, processing, transmitting and retransmitting telephone or telegraph signals

E. In 2000, chapter 63 of the Laws of 2000 (part S, section 7) added a new paragraph 12-a to Tax Law § 1115(a) which provided that, effective September 1, 2000, receipts from the following shall be exempt from sales and use taxes:

Tangible personal property for use or consumption directly and predominantly in the receiving, initiating, amplifying, processing, transmitting, retransmitting, switching or monitoring of switching of

telecommunications services for sale or internet access services for sale or any combination thereof. Such tangible personal property exempt under this subdivision shall include, but not be limited to, tangible personal property used or consumed to upgrade systems to allow for the receiving, initiating, amplifying, processing, transmitting, retransmitting, switching or monitoring of switching of telecommunications services for sale or internet access services for sale or any combination thereof. As used in this paragraph, the term ‘telecommunications services’ shall have the same meaning as defined in paragraph (g) of subdivision one of section one hundred eighty-six-e of this chapter.

The term “tangible personal property” means corporeal personal property of any nature having a material existence and perceptibility to the human senses (Tax Law § 1101[b][6]; 20 NYCRR 526.8[a]).

The definition of “telecommunication services” set forth in Tax Law § 186-e(1)(g)³ provides as follows:

‘Telecommunication services’ means telephony or telegraphy, or telephone or telegraph service, including, but not limited to, any transmission of voice, image, data, information and paging, through the use of wire, cable, fiber-optic, laser, microwave, radio wave, satellite or similar media or any combination thereof and shall include services that are ancillary to the provision of telephone service (such as, but not limited to, dial tone, basic service, directory information, call forwarding, caller-identification, call-waiting and the like) and also include any equipment and services provided therewith. Provided, the definition of telecommunication services shall not apply to separately stated charges for any service which alters the substantive content of the message received by the recipient from that sent.

At the same time, chapter 63 of the Laws of 2000 removed from Tax Law § 1115(a)(12), the language set forth in Conclusion of Law “D”.

F. First, while it appears that Concentric has abandoned its argument that its purchases from MCI Worldcom, Eagle Communications and Frontier are exempt from tax as sales for

³ This definition was added to the Tax Law by chapter 2 of the Laws of 1995 and became effective on January 1, 1995.

resale, it is clear that Concentric did not make these purchases for resale. Concentric, admittedly, is an internet service provider and, as such, does not sell telephone or telegraph services to its customers. As noted by the Tax Appeals Tribunal in *Matter of Phone Programs, Inc.* (Tax Appeals Tribunal, April 6, 2000), “the resale exclusion for utility services demands that the services be resold as utility services, i.e., telephone services (20 NYCRR 526.6[c]; 527.2[e]).”

G. The next issue which must be considered is whether Concentric’s purchases from MCI Worldcom, Eagle Communications and Frontier, which are the subject of this refund claim, are telephony or telephone service. The primary obstacle in addressing this issue is the confusion over exactly what it was that Concentric purchased, i.e., did it, as the Division claims, purchase intrastate telephone service from these providers or did it, as Concentric asserts, purchase line access to provide its customers with internet access via a packet switched network which is distinguishable from sound reproduction networks. In essence, the Division contends that Concentric’s use of the telephone lines to provide internet access is irrelevant. Concentric, on the other hand, states that the Division improperly categorized these purchases as intrastate telephone services because the lines constitute access points to a packet switched network. While Concentric acknowledges (*see*, Petitioner’s Reply Brief, p. 5) that the T-1 and ATM lines which it purchased could be used for traditional telephone lines and that the lines begin and end in the State of New York, it maintains that it did not use the lines to transmit signals and, therefore, did not use the lines to provide telephone service.

As previously noted (*see*, Conclusion of Law “B”), Tax Law § 1105(b) imposes the tax “on receipts from intrastate communication by means of devices employing the principles of telephony and telegraphy.” While Concentric did not use the lines to transmit traditional

telephone signals, admittedly, the lines could have been used for that purpose. 20 NYCRR 512.2(a)(2) clearly states that the words “of whatever nature” contained in the statute which imposes the tax (Tax Law § 1105[b]) indicate that “a broad construction is to be given the terms describing the items taxed.”

It must be noted that the sales tax is a “transaction tax,” i.e., the liability for the tax occurs at the time of the transaction (*see*, 20 NYCRR 525.2[a][2]). At the time of its purchases, Concentric was a retail customer of MCI Worldcom, Frontier and Eagle Communications and what it purchased from these vendors was apparatus which could be used “for transmission of sound, sound reproduction or coded or other signals” (20 NYCRR 527.2[d][2]). The fact that Concentric, subsequent to its purchase of the lines, used such lines to provide its customers with internet access via a packet switched network and did not utilize them for sound reproduction does not render the purchases nontaxable. Moreover, the Division, in a memorandum of its Technical Services Bureau (TSB-M-97[1.1]C, TSB-M-97[1.1]S) dated November 15, 1999, stated, in relevant part, as follows:

Thus, the purchase of telephone service from telecommunications providers (such as local exchange companies or long-distance companies) to access the Internet does not fall within the scope of this exemption.⁴ For example, the charge for the telephone call to an ISP to initiate access to the Internet is still subject to both sales tax and the telecommunications excise tax, *as is the charge to an ISP for leasing telephone lines from a telecommunications provider* (emphasis added).

It is hereby determined, therefore, that Concentric’s purchases of line access from MCI Worldcom, Frontier and Eagle Communications were properly held by the Division to be purchases of telephony or telephone service.

⁴ The exemption referred to in the memorandum is that set forth in Tax Law § 1115(v) which exempted from sales tax the receipts from the sale of internet access service and the use of such service. This exemption was added by chapter 615 of the Laws of 1998 (*see*, Conclusion of Law “C”).

H. Concentric's alternative argument is that even if held to be purchases of telephony or telephone services, its purchases of line access are nevertheless exempt from tax because such lines are component parts of Concentric's interstate product known as internet access. As indicated in Conclusion of Law "A", the statute imposing the tax (Tax Law § 1105[b][1][B]) specifically excludes from tax interstate and international telephony and telegraphy and telephone and telegraph service. Concentric asserts that in all cases the internet traffic on its network, while originating in New York, was routed through Washington, D.C. or Chicago, Illinois before reaching its destination. In support of its position, Concentric cites to *Matter of Southern Pacific Communications Co.* (Tax Appeals Tribunal, May 14, 1991) wherein the Tribunal stated that in determining whether a taxpayer's activities are involved in interstate commerce, it is improper to isolate and individually examine the separate components of the overall activity being engaged in by such taxpayer. Concentric states that the T-1 and ATM lines which are the subject of this refund claim when integrated with other network components (such as servers, routers and modems) form an interstate internet network. Since the line access is just one component part of interstate internet access, Concentric contends that it cannot be subject to tax.

In response, the Division states that the line access services were delivered to and consumed by Concentric in its New York State locations. Unlike the petitioner in *Southern Pacific (supra)*, Concentric did not provide interstate telephone services to its customers. Instead, the line access services were used to provide a service which is not subject to tax, i.e., internet access service.

For each of the purchases of Concentric which are at issue herein, the line access service was delivered to and consumed by Concentric at various locations in New York State (*see*,

Finding of Fact “3”). Simply because the internet traffic on Concentric’s network was routed out of state, i.e., through Washington, D.C. or Chicago, Illinois, does not, in and of itself, lead to the conclusion that what Concentric purchased was *interstate* telephony or telephone service.

Unlike the taxpayer in *Southern Pacific (supra)*, Concentric was not in the business of selling an interstate telephone service; in fact, it sold no telephone service at all. Concentric was the purchaser of the line access and it used the lines to provide an entirely separate service, internet access service, which, pursuant to Tax Law § 1115(v), was exempt from sales tax for the period at issue herein.

In Concentric’s reply brief it states that if, as the Division argues, line access purchases constitute telephony, then line access must be considered an interstate variety of telephony. Based upon the record in this matter, Concentric’s argument is without merit since the line access purchases at issue in this matter were all located within New York State. While the lines may well have been used to provide internet access service of an interstate nature to Concentric’s customers, the taxes for which this petitioner seeks a refund were not imposed upon the internet service but upon the intrastate line access charges only.

Matter of Callanan Marine Corp. v. State Tax Commn. (98 AD2d 555, 471 NYS2d 906, *lv denied* 62 NY2d 606, 479 NYS2d 1026) is a case which involved sales tax imposed upon scows which delivered crushed stone to locations within New York State. The taxpayer transported the crushed stone from quarries located near Kingston, New York down the Hudson River to New York City. However, for a portion of the trip, the scows proceeded on the New Jersey side of the Hudson River for navigational reasons for approximately 20 miles. Petitioner argued that the scows were engaged in interstate commerce because they crossed state lines. The Court disagreed stating that the scows had a New York origin and a New York destination and

that passage through New Jersey waters was merely incidental to what was clearly an intrastate journey.

In *Matter of Western Union Telegraph Company* (State Tax Commission, February 4, 1983 [TSB-H-83(57)S]), the Commission held that telegraphic messages which originated and terminated in New York but which passed through a computer complex in New Jersey was intrastate telegraphy subject to sales tax under Tax Law § 1105(b).

Later in the reply brief, Concentric asserts that line access is only one component part of internet access which is an interstate network and, therefore, the line access component of internet access cannot be subject to sales tax. What Concentric appears to be conveniently overlooking is the fact that the tax is not being imposed on the internet access which is an interstate activity and which, pursuant to Tax Law § 1115(v), is exempt from tax. The purchase of the telephone line access by Concentric from its various vendors was the act that triggered the imposition of the tax and the fact that Concentric subsequently used the line access to provide a nontaxable interstate service to its customers does not affect the taxability of the preceding transactions, i.e., the purchase of the line access by Concentric from its vendors.

I. It must be noted that in its original claim for refund, Concentric alleged that the tax for which the refund was being sought was imposed and paid not only on line access charges, but on tangible personal property, including equipment, used in connection with its delivery of internet services. As previously noted (*see*, Finding of Fact “3”), the summary of the invoices upon which the refund claim was based indicates that what was actually purchased was some type of line access. In its brief and reply brief, Concentric concedes that the subject purchases were for line access. At the hearing, Concentric’s expert witness, Michael Scott, was unable to identify each of the items contained on various invoices.

This is noteworthy because if Concentric purchased tangible personal property such as equipment in conjunction with its purchases of line access, it is likely that some or all of that equipment could have been exempt from sales tax. For periods prior to September 1, 2000, Tax Law § 1115(a)(12) exempted certain telephone equipment and for periods after September 1, 2000, Tax Law § 1115(a)(12-a) exempted certain tangible personal property for use or consumption directly and predominantly in internet access services for sale.

However, as correctly noted by the Division, all sales of tangible personal property are presumed to be taxable unless the contrary is established and the burden of proving entitlement to an exemption from tax is upon petitioner (*Matter of Surface Line Fraternal Org. v. Tully*, 85 AD2d 858, 446 NYS2d 451). In the present matter, Concentric failed to produce sufficient evidence (other than invoices the contents of which even its expert witness had difficulty in clearly identifying) to sustain its burden of proving that what it purchased was exempt from tax under the aforesaid provisions of the Tax Law.

I. The petition of Concentric Network Corporation is hereby denied.

DATED: Troy, New York
January 20, 2005

/s/ Brian L. Friedman
ADMINISTRATIVE LAW JUDGE